ADDENDA CAPITAL

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Going from Win-Win to Win-Lose, or Worse, to Lose-Lose

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The current US administration's international trade strategy based on basic populism is etched in a dated win-lose negotiating framework espoused by its current leader. This approach to negotiations takes us back to a time before nations came to understand the benefits of free trade based on the comparative advantage economic theory. Simply put, this theory concludes that the specialized production that results from the optimal allocation of resources, when traded, leads to welfare gains.

The global economy generally followed that principle after the second world war leading to the integration of the global economy and to an unprecedented period of growth. Though welfare gains were spectacular, leading millions out of poverty and many to prosperity, there was collateral damage along the way, notably the unequal division of the spoils that are now at the root of the populist movements we see across many, and mostly industrialized, nations.

This first salvo of a trade war does not augur well for the health of the global economy nor for equity markets' stability around the globe. On the rates front, impediments to trade will likely lead to higher prices and slower growth, leaving central banks in a "catch-22" situation that will probably weigh on their resolve to increase policy rates.

It may be too late for the current upheaval in markets to trigger a change away from populist governments in the short run. As time goes by however, consumers will end up paying higher prices for the goods that have been targeted by the new tariffs. Voters could then decide to come back to the win-win framework they will have missed and hope that governments will come back to their senses and move away from the dangerous path of protectionism.